

**UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

California Independent System Operator Corporation) Docket No. ER12-1856-000

**ANSWER TO MOTIONS TO INTERVENE AND COMMENTS,
MOTION TO FILE ANSWER, AND ANSWER TO PROTESTS, OF THE
CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION**

The California Independent System Operator (“ISO”) submits this Motion for Leave to File Answer¹ and Answer to address protests and comments filed in response to the ISO’s tariff amendments filed May 25, 2012, in compliance with Order No. 741. The Commission received thirteen motions to intervene.² Of those thirteen pleadings, four included at least limited protests – those of SVP/MSR, CMUA, NCPA, and the Six Cities. The entities filing these four protests are referred to collectively as “the protesters.”

For the reasons explained below, the Commission should deny the protests with one limited exception. The ISO proposes to add a sentence to

¹ The ISO submits this answer pursuant to Rules 212 and 213 of the Commission’s Rules of Practice and Procedure, 18 C.F.R. §§ 385.212, 385.213. The ISO requests waiver of Rule 213(a)(2), 18 C.F.R. § 385.213(a)(2), to permit it to make an answer to the protests. Good cause for this waiver exists here because the answer will aid the Commission in understanding the issues in the proceeding, provide additional information to assist the Commission in the decision-making process, and help to ensure a complete and accurate record in the case. See, e.g., *Xcel Energy Services, Inc.*, 124 FERC ¶ 61,011, at P 20 (2008); *California Independent System Operator Corp.*, 132 FERC ¶ 61,023, at P 16 (2010); *Equitrans, L.P.*, 134 FERC ¶ 61,250, at P 6 (2011).

² Motions to intervene were filed by the following parties: the California Department of Water Resources State Water Project, Calpine Corp., the California Municipal Utilities Association (“CMUA”), the City and County of San Francisco Public Utilities Commission, J.P. Morgan Energy Ventures Corp., Macquarie Energy LLC, the Modesto Irrigation District, the Northern California Power Agency (“NCPA”), the NRG Companies, Pacific Gas and Electric Company, the City of Santa Clara together with the M-S-R Power Agency (“SVP/MSR”), and the “Six Cities” of Anaheim, Azusa, Banning, Colton, Riverside and Pasadena.

proposed section 11.29(a) at the request of the Six Cities based on their concern about the tax-exempt status of their transmission facilities.

I. Issues Raised by Protestors

A. Tax-Exempt Status of Certain Generation and Proposed Carve-Out for Bilaterals and Self-Supply

Each of the protestors raises concerns about “private use” restrictions associated with tax-exempt financing for certain generation projects, and whether having the ISO as a counterparty would violate those restrictions.³ NCPA observes that “[d]uring the abbreviated stakeholder process, [it] was unable to determine the potential tax impacts” of the tariff amendments.

NCPA notes that, since the conclusion of the stakeholder process, it “has been able to engage in more extensive discussions with bond counsel, and has become somewhat more optimistic.”⁴ Specifically, NCPA believes that “the proposal may not present a serious problem for its already-financed projects.”⁵ The ISO itself has looked carefully at this issue, and believes that sales to the ISO as counterparty do not violate “private use” restrictions in the tax-exempt bonds. The ISO will continue to work with the protesters to help resolve their concerns.

In addition, the solution proposed in the protests is not a viable option for the ISO. The protests cite language in PJM’s tariff to the effect that PJM is not a

³ The most detailed explanation of the concern can be found in NCPA at 4-5.

⁴ NCPA at 6.

⁵ *Id.*

counterparty to self-supply or bilateral transactions, and ask the Commission to require the ISO to adopt the same language.⁶ The PJM market, however, differs from the ISO's in a way that precludes the proposed solution. Unlike the ISO, PJM has an explicit mechanism that allows market participants to settle the energy components of sales and purchases bilaterally, rather than through the central settlement and clearing system.⁷ It is these transactions that take place outside the ISO that are the "bilateral" and "self-supply" transactions for which PJM does not serve as counterparty.⁸ Without a similar mechanism for excluding such transactions from its central settlement and clearing function, the ISO cannot simply state that it is not counterparty to these transactions. That would exclude significant portions of the ISO's financial settlements from the central counterparty structure, thereby undermining the purpose of Order 741.⁹

As an alternative, the Six Cities propose a "reopener" provision, under which the tariff would be "immediately modified to include appropriate exceptions" if "market participants receive notice concerning the possibility of

⁶ See CMUA at 7; NCPA at 5-6; Six Cities at 3-6. The Six Cities also cite MISO as an example. MISO's market is structured like PJM's, offering "financial schedules" that are similar to PJM's eSchedules.

⁷ Regarding PJM's "eSchedules," see <http://pjm.com/training/~/media/training/core-curriculum/ip-transactions-201/transact-201-internal-transactions-eschedules.ashx> and <http://pjm.com/~/media/etools/eschedules/pjm-eschedules-user-guide.ashx>.

⁸ See PJM Operating Agreement, Schedule 1, Section 1.7.10(a)(i) (noting that "Such bilateral contracts shall be ... shall be reported to and coordinated with the Office of the Interconnection ... pursuant to the LLC's rules relating to its eSchedules ...") and 1.7.10(a)(ii)(noting that PJM is not counterparty to the bilateral transactions).

⁹ As SVP/MSR points out, the ISO has proposed to exclude sales to purchasers located in Mexico from the central counterparty structure. See SVP/MSR at 8. That exclusion, however, is necessary for the ISO to comply with Mexican law. The proposed exclusion, in contrast, does not appear to be necessary for the protestors to comply with restrictions necessary for tax-exempt financing or federal preference power, as explained in the text above.

adverse actions related to their tax-exempt financing.”¹⁰ The ISO appreciates the importance to the protesters of maintaining tax-exempt status for their projects, and remains committed to working with them to resolve their concerns. At this point, however, there is not a detailed proposal to which the ISO can respond.

B. Preference Power from Federal Power Marketing Agencies

The protesters raised concerns during the ISO’s stakeholder process about restrictions associated with preference power from federal power marketing agencies. Specifically, they were concerned that having the ISO as counterparty for transactions involving preference power might violate a prohibition on reselling that power.¹¹

The central counterparty language is not intended to affect transactions involving preference power. Moreover, as the protesters note,¹² Western addressed the concern in a letter dated June 6, 2012. Western’s letter, which is included with the protests of SVP/MSR and NCPA, states that Western participated in the ISO’s stakeholder process, reviewed the proposed tariff amendment, and that it believes that transactions with the ISO as counterparty will not violate the agreements Western has with its preference power customers. Specifically, Western’s letter states:

when Western acts as the SC for the BR [Western’s Base Resource], even if the CAISO is a central counterparty to the schedules, Western does not consider this specific transaction a violation of the resale provisions of the GPCP [General Power Contract Provisions]. Similarly, if

¹⁰ Six Cities at 10-11.

¹¹ NCPA at 7; SVP/MSR at 7; CMUA at 8-9; Six Cities at 2-9.

¹² NCPA at 8; SVP/MSR at 8; CMUA at 8-9; Southern Cities at 8 n.6.

a Central Valley Project customer, such as the Northern California Power Agency, is acting as an SC and schedules BR to its members in the CAISO, Western does not consider this initial transaction (and this initial transaction only) to its members a resale in violation of the GPCP, even if the CAISO is a central counterparty to the schedules.¹³

This letter resolves the protestors concerns about federal preference power from Western. Accordingly, the ISO submits that it is not necessary to grant the protestors any other relief related to preference power.

In the letter, Western reserves the right to change its position “as the CAISO’s tariff evolves.”¹⁴ Any action that may become necessary in the future to preserve market participants’ right to federal preference power in light future tariff amendments can be addressed when those tariff amendments are proposed.

One protest states that Western’s letter, while helpful, “does not dispose of the issue conclusively,” because it “does not insulate Western or its customers from judicial challenge.”¹⁵ This protest, however, does not provide any detail about how such a challenge could arise, nor does it identify an applicable law or regulation that could form the basis for such a challenge. The unsupported assertion that the letter from Western might be legally erroneous, to the extent that is being suggested, is not a sufficient basis to reject the proposed tariff amendments.

¹³ NCPA Attachment A (second full paragraph).

¹⁴ *Id.* (second-to-last line).

¹⁵ CMUA at 9.

C. State Greenhouse Gas Regulation

During the ISO's stakeholder process, a range of stakeholders expressed concern that, by becoming counterparty to market transactions, the ISO might become liable for procuring emissions allowances under California's state program regulating greenhouse gas emissions. The protesters note that the ISO believes it has resolved this issue by specifying in its proposed tariff language that it may not be listed as the "Purchasing Selling Entity" on e-Tags.¹⁶ None of the protests fault the ISO's solution. They do state that "regulatory uncertainty remains" because the state regulation is new,¹⁷ but ask only that the ISO work with the California Air Resources Board to ensure that it does not become liable for emissions allowances as a result of becoming a counterparty.

The ISO has been working with the Air Resources Board to this end, and will continue to do so.

D. State Renewable Portfolio Standards.

The NCPA and SVP/MSR note that the conversion to central counterparty status may have implications for their compliance with California law governing renewable generation portfolios. As the NCPA explains, a sale of renewable energy to the ISO "could break the unbundled nature of the product that the regulations require," causing market participants to lose relevant credits and thereby incur substantial costs.¹⁸

¹⁶ See the ISO's May 25, 2012 Transmittal Letter, at 6.

¹⁷ NCPA at 9, SVP at 9, CMUA at 6.

¹⁸ NCPA at 9-10; see also SVP at 9.

The NCPA and SVP/MSR seek no relief from the Commission – just a commitment from the ISO that it will “continue to work with stakeholders and the relevant state agencies to address any problems that result.”¹⁹ The ISO plans to do so.

SVP/MSR, however, seeks clarification of proposed section 4.5.3.2.2, reflecting that the ISO, though a counterparty to the transactions in its markets, will not be in the chain of title on delivery. SVP/MSR are concerned that this language might be misconstrued as applying to interchange transactions only:

CAISO's change to its proposed Section 4.5.3.2.2, indicating that CAISO does not take title, is housed within a provision addressing intertie transactions. The corresponding provisions for transactions within the CAISO Grid are silent as to title transfer. Although it is difficult to comprehend how or why CAISO would structure transactions within its Grid differently than imports, the location of the provision, and the lack of a parallel statement with regard to transactions at points within the CAISO Grid, create confusion and uncertainty. The Commission should direct CAISO to clarify that it is not taking title under any transactions, not just those at the interties.²⁰

The ISO did not intend to limit the following language in proposed section 4.5.3.2.2 to intertie transactions, but rather intends that it will apply generally to delivery of energy into, on and through the ISO-controlled grid:

title to Energy shall pass directly from the entity that holds title when the Energy enters the CAISO Controlled Grid to the entity that removes the Energy from the CAISO Controlled Grid, in each case in accordance with the terms of this CAISO Tariff.

The ISO believes this language is sufficiently clear.

¹⁹ SVP at 10; see also NCPA at 10.

²⁰ SVP/MSR at 10.

E. Tax-Exempt Status of Transmission Facilities

The Six Cities, who are the only protesters that are also participating transmission owners, express a concern that the change might have implications for the tax-exempt status of their transmission facilities.²¹ Accordingly, they “request that the CAISO Tariff be modified to provide that the new central counterparty rules are not intended to affect the tax-exempt status of these transmission facilities.”²²

The ISO agrees to add the requested tariff language to section 11.29(a). Specifically, the ISO proposes to add a subsection (iii) which states:

The CAISO’s status as contracting counterparty is not intended to affect the tax-exempt status of transmission facilities or entitlements subject to the CAISO’s operational control.

F. Sales Taxes Owed by Market Participants

To ensure it is not exposed to certain state taxes, the cost of which would have to be passed on to market participants, the ISO will be requiring market participants to provide resale certificates.²³ SVP/MSR state that they may need the same in return from the ISO:

If sales tax resale certificates are necessary for CAISO to demonstrate that its sales to market participants are exempt from sales taxes, then it is likely that CAISO needs to provide the same certificates to market participant sellers so they can demonstrate their sales to the CAISO are exempt from sales tax as sales for resale.

²¹ Six Cities at 9-10.

²² *Id.* at 9.

²³ SVP/MSR at 11; see also proposed tariff section 4.5.3.14.

SVP/MSR ask the Commission to direct the ISO to provide such resale certificates.²⁴

The ISO opposes any such requirement at this point, because SVP/MSR have not provided enough detail to justify it. SVP/MSR may be exempt from sales taxes for any number of other reasons, which would make the proposed requirement unnecessary. With that said, the ISO will, if requested, work with market participants to document its own status as a reseller so that market participants do not unnecessarily incur state taxes.

G. ISO as Debt Collector for the Market

The SVP/MSR protest observes that the proposed tariff amendment grants the ISO the exclusive right to collect on behalf of the market in the event of a default. They explain that this change could potentially limit their rights as creditors in the bankruptcy proceeding of a defaulting market participant.²⁵

The Commission should deny this protest, for three reasons. First, SVP/MSR do not propose any changes to the ISO's tariff amendments. Second and more important, the ISO assumption of responsibility for collecting market defaults is central to the Commission's purposes in Order 741. As the counterparty to the bankrupt market participant, the ISO will be in the best position to collect, because it will be the only party in a position to set off amounts that would otherwise be owed to the debtor on those transactions.

Third, in the unlikely event the ISO's role as debt collector did deprive a market participant of important legal rights, other solutions may be available. As

²⁴ SVP/MSR at 11.

²⁵ *Id.*

the ISO understands the concern, SVP/MSR may want standing to contest the plan of reorganization of another utility that has filed for bankruptcy. If that were important, and yet SVP/MSR (or any other market participant) did not have a claim against the bankruptcy utility except through the ISO's market, the ISO could explore the possibility of entering an agreement to assign a portion of the ISO's claim. Such an agreement might have to be approved by the Commission, because it would require the assignee to forego rights that it would otherwise have under the ISO's tariff to a portion of any amounts collected by the ISO. As the counterparty, however, the ISO would have the ability to work toward this type of solution.

II. Conclusion

For the reasons explained above, the Commission should accept the tariff amendments as filed in this proceeding, subject only to the tariff revision discussed at page 7 above (proposing to add text to section 11.29(a)(iii)).

July 3, 2012

Respectfully submitted,

/s/ Daniel J. Shonkwiler

Nancy Saracino
General Counsel
Roger E. Collanton,
Assistant General Counsel
Daniel J. Shonkwiler
Senior Counsel
California Independent System
Operator Corporation
250 Outcropping Way
Folsom, CA 95630
Tel: (916) 351-4400
Fax: (916) 351-4436
dshonkwiler@caiso.com

Certificate of Service

I hereby certify that I have served the foregoing document upon all of the parties listed on the official service list for the above-referenced proceeding, in accordance with the requirements of Rule 2010 of the Commission's Rules of Practice and Procedure (18 C.F.R. § 385.2010).

Dated at Folsom, California this 3rd day of July, 2012.

/s/ Anna Pascuzzo
Anna Pascuzzo